

Markit iTraxx[®] Japan Index Rules

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Index Overview

Markit Credit Indices are indices that track different segments of the debt markets (corporate, municipal and sovereign debt bonds and/or loans) across different regions (Europe, Asia, North America and Emerging Markets) and are referenced in various tradable products such as credit default swaps (“CDS”)

Markit Credit Indices are made up of the most liquid entities in the relevant single-name CDS market.

The indices roll on a semi-annual basis, and the composition of each new series (a new index) is established based on a transparent set of rules designed to ensure that the current series tracks the most liquid instruments in the relevant market.

Markit iTraxx Japan Index

The Markit iTraxx Japan Index is composed of forty (40) liquid Japanese entities with investment grade credit ratings that trade in the CDS market.

The Markit iTraxx Japan Index is a tradable index that allows market participants to take a view on the overall credit quality and direction of the underlying basket by trading one instrument.

All Markit iTraxx Indices are owned, managed, compiled and published by Markit Indices Limited.

Administrator

Markit is the Administrator of the Markit iTraxx Japan Index. The composition of this index is determined by the Administrator in accordance with the rules and methodologies set forth in this document (the “Rules”).

The Administrator has sole responsibility to interpret the Rules. The Administrator shall make determinations and perform all actions regarding the index pursuant to the Rules provided that upon the occurrence of an event that the Administrator determines materially impacts the integrity of one or more type of Markit iTraxx Japan Index-related transactions, including but not limited to trading interruptions; market instability; and/or force majeure events, the Administrator, acting in a commercially reasonable manner, may at its sole discretion determine that it is appropriate to depart from the methodologies, timelines and/or procedures set forth in the Rules to obtain a result that preserves the economic intent of such Markit iTraxx Japan Index. Where the best course of action is not clear Markit will consult the Index Advisory Committee for guidance prior to making any such determination. The determined course of action will be documented, communicated to all stakeholders and published on the Markit website www.markit.com/Product/Indices under the iTraxx News page.

In the event that any critical input required in the construction of a new series of the index is not available, Markit will confer with the Index Advisory Committee and publish the outcome of any material change as well as any decisions taken at Markit’s discretion that have led to a methodology change.

Roll Dates

Markit iTraxx Japan Index will begin on March 20 (or the Business Day immediately thereafter in the event that March 20 is not a Business Day) and September 20 (or the Business Day immediately thereafter in the event that September 20 is not a Business Day) of each calendar year (each such date, a “Roll Date”).

All references to “Business Days” in this document mean days on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealings in foreign exchange and foreign currency deposits) in Tokyo, Japan. All times referred to in this document, refer to local time in Tokyo, Japan.

Rule Revision

The rules for the index are reviewed semi-annually prior to the index roll. Decisions made following an index rule review will be communicated to stakeholders via e-mail and published on the Markit website. The publication will contain an overview and timelines for implementation of such rules changes.

Maturity

Each Index that has a Roll Date of March 20 shall be issued with the maturity date of June 20 occurring 5 years following the Roll Date.

Each Index that has a Roll Date of September 20 shall be issued with the maturity date of December 20 occurring 5 years following the Roll Date.

Weighting

Each constituent in the Markit iTraxx Japan Index will have equal or approximately equal weightings. The weighting of each entity will be equal to (i) one divided by (ii) the number of entities in such index, expressed as a percentage with three decimal places (e.g., 3.226%). In the case where rounding is necessary to express the weightings in this manner, the entities shall be arranged in alphabetical order, with the weightings of the entities at the top of the list being rounded up to the nearest one-thousandth of a percent and the weightings of the entities at the bottom of the list being rounded down to the nearest one-thousandth of a percent until the weightings of all entities have been rounded and the aggregate of the weightings equals exactly 100%.

Relevant Rating

Determinations of constituents for the Markit iTraxx Japan Index will be based, in part, on the “Relevant Rating” of each entity in consideration for inclusion or exclusion. For the purposes of these Rules, “Relevant Rating” means the highest rating of the following:

1. Higher of the Issuer Rating, Senior Unsecured Debt Rating, and Corporate Family Ratings for Moody's;
2. Higher of the Long-term Issuer Credit Rating and Senior Unsecured Debt Rating for S&P;
3. Higher of the Issuer Default Ratings and Senior Unsecured Debt Rating for Fitch.
4. The Rating and Investment Information, Inc. (R & I) Issuer Rating
5. The Japan Credit Rating Agency, Ltd. (JCR) Long Term Issuer Rating

Entities must have a Relevant Rating of at least BBB-/Baa3 by one of the rating agencies listed above in order to be classified as Investment Grade.

Rating changes that could affect the index membership are taken into account if the Administrator is notified of such change prior to 5:00 pm Tokyo time on the second Friday of the month in which the Roll Date occurs.

General Criteria.

- Entities must be Investment Grade.
- Entities must demonstrate trading activity greater than zero during the last eight weeks preceding the last Friday of the month prior to the Roll Date as measured in the DTCC 6 Month Analysis Top 1,000 Single Names Report (see below)
- Entities must be incorporated in Japan.
- If a company is guaranteed by or guarantees another one, only the most liquid is eligible.
- Volumes for separate entities that fall under the same trading ticker, but trade separately in the CDS market, are summed to arrive at an overall volume for each ticker. The most liquid entity under the ticker is eligible for index membership.
- Index Sector Limits – The Index is subject to a maximum of 12 entities from any of the 6 Nikkei Stock Average sector categories, consolidated from the 36 Nikkei industrial classifications.
- Financial Entities that trade under the ISDA Transaction Type ‘Japan Financial Corporate’ as specified by Markit RED are not eligible for selection.

Creation of the Liquidity List

Following publication of the DTCC 6 month Analysis Top 1,000 Single Names Report or any successor report thereto published by DTCC, or if such report is no longer available a successor report that measures liquidity within the CDS market (collectively known as the “**DTCC Report**”) This report measures liquidity over the last six months preceding the last Friday of the month prior to the Roll Date.

The Administrator will create a Liquidity List based on the average weekly trading activity as measured in the DTCC Report.

Entities on the Liquidity List should satisfy the General Criteria.

The list is then ranked according to trading volumes, i.e. the entity with the highest trading volume is ranked #1.

If there are less than 40 eligible entities available from the Liquidity List constructed using DTCC data Markit will initiate a liquidity poll whereby market participants will be requested to send a list of the most liquidly traded entities which are not included in the *DTCC 6 Month Analysis Top 1,000 Single Names* report:

- Trading volumes of each entity should be aggregated by market participants.
- Trading volumes for the past 6 months from the last Tokyo Business Day of the month prior to the roll date should be used.
- All internal transactions are excluded from the volume statistics, e.g. those with internal proprietary trading desks.

The Administrator will then aggregate the volume ranked lists from market participants to compute final liquidity ranking for each entity which will be added to Liquidity List, below the names for which DTCC data was available.

Creation of the New Index Series

At the time of an index roll, the index composition is initially set to be the same as the previous series, the Administrator will then identify entities which match the Roll Exclusion criteria below and remove them from the existing index. The Administrator will then add new and replacement entities by applying the Roll Inclusion criteria to create the new index. The inclusion and exclusion processes are as described below

Roll Exclusions

No later than eight (8) Business Days prior to a Roll Date, the Administrator will create list of entities in the current index that no longer satisfy the General Criteria set forth above or match the exclusion criteria set forth below:

- **Corporate Events.** The Administrator may determine, at its sole discretion and based on publicly available information, that a corporate event has occurred or been announced in relation to any current constituent that renders such current constituent unsuitable for inclusion. For purposes of this paragraph,
 - (i) "Corporate Events" include mergers, acquisitions or other similar events and
 - (ii) "Publicly available information" includes, but is not limited to, information from public filings, financial reports, or information published in the main sources of business news in the country in which the corporate entity is organized and any other internationally recognized published or electronically displayed news services.
- **Credit Events.** The Administrator may determine at its sole discretion that a current constituent is no longer suitable for inclusion in the Index if one of the following occurs on or after the previous Index Roll Date with respect to any current constituent:

- (i) a notice is published on the ISDA Credit Derivatives Determinations Committee webpage (<http://dc.isda.org/>, or any successor webpage thereto) announcing that a request relating to a potential Credit Event (as defined in the Credit Definitions) in respect of such current constituent has been accepted by the relevant Credit Derivatives Determinations Committee (as defined in the Credit Definitions, the "DC"); provided that as of 5:00 p.m. Tokyo time on the first business day following the day on which the relevant DC is required to convene to consider such request under the DC rules (such timeline to be determined without regard to any ability of the DC to amend the published timetables set forth in the DC rules immediately prior to such request), a DC No Credit Event Announcement (as defined in the Credit Definitions) has not occurred and no announcement to the effect that such request has been dismissed, withdrawn, or rejected by the relevant DC has been published on such webpage; or
 - (ii) a DC Credit Event Announcement (as defined in the Credit Definitions) occurs with respect to such current entity. As set forth in these Rules, the Administrator may consider any information and make any determinations necessary under this Roll Exclusion to obtain a result that preserves the integrity of the Index.
- **Liquidity Based Exclusion;** Existing entities in the current index will be excluded from the new index if they are either not part of the Liquidity List or if more than 75 entities are available on the Liquidity List, and they are ranked at #76 or lower.
 - **Spread Based Exclusion;** Entities priced at greater than 50 points upfront (corresponding to a 100 bps fixed coupon) for the 5Y tenor will be excluded. The average upfront over the last 10 Tokyo Business Days of the month prior to the Roll Date will be considered.^[1]

These entities will be replaced by the most liquid eligible new entities from the Liquidity List subject to the inclusion criteria set forth below. Current entities identified in accordance with the above are "Roll Exclusions."

^[1]Where credit default swap spreads are required to determine eligibility for inclusion, the "Markit CDS End of Day" service will be used. Markit receives contributed CDS data from market participant's official books of record. This data undergoes a rigorous cleaning process before being aggregated to form the "Markit CDS End of Day" Composite

Roll Inclusions

Using the Liquidity List the Administrator will identify entities that match the criteria below to create a list of entities that are not current constituents, that are not subject to any Roll Exclusion criteria above, and that satisfy the General Criteria:

- **Liquidity Based Inclusion;** New entities ranked #25 or higher are included automatically. If the inclusion causes the maximum 12 entity per sector limit to be exceeded, the least liquid entity from that sector is then excluded, otherwise the least liquid entity from the existing overall 40 entity list is excluded.
- If an existing constituent has been excluded from the new index due to the Roll Exclusions above, the entity will be replaced by the most liquid new entity from the Liquidity List, subject to the index sector limits. (If the replacement entity belongs to a sector which already has 12 entities, the next most liquid entity from the liquidity list from a sector containing 11 or less entities is selected).
- This process is repeated until all Roll Exclusions have been replaced and the index has 40 entities which satisfy the 6 sector limits.

Publication of Provisional Markit iTraxx Japan Index

The list of entities resulting after the steps above (the “Provisional Markit iTraxx Japan Index”) will be published on Markit’s public web site for comment no later than seven (7) Business Days prior to the Roll Date. The Administrator will review comments received and determine whether amendments are necessary. The Administrator welcomes public comment, but is not required to follow or otherwise address any comment received. The Administrator will publish the expected name changes (if any) on its public website as it determines such changes are required. The comment period will end four (4) Business Days prior to the Roll Date. The draft and final annexes for the Markit iTraxx Japan Index will be published as set forth below.

Reference Obligations

The reference obligations for the reference entities are obtained from Markit Group’s Reference Entity Database (RED) in conjunction with input from Markit iTraxx Japan Index market participants. For names in the overall index, senior reference obligations are used where possible.

Coupon Levels and Recovery Rates

No later than two (2) business days preceding the roll date, a telephone poll is initiated by the Administrator to determine the coupons and recovery rates for each index. Coupon levels are rounded to the nearest 5 basis points and recovery levels to the nearest 5%.

Final Review of Constituent List

On any day prior to the date of publication of a final index annex, the Administrator may determine that any entity that is intended to be included in the relevant index fails any of the criteria specified in the General Criteria and Roll Exclusions section, such entity shall be excluded from the Index. If the Administrator determines that any entity shall be excluded from the Index in accordance with this Final Review of Constituent List, then the highest ranked entity in the Liquidity Rankings that has not already been included in the Index and that will not cause a sector limit to be exceeded, shall be added to the new Index, respectively, as a replacement entity.

Where a determination with regard to constituent selection is made by the Administrator which involves discretion and/or expert judgement, Markit will consult the Index Advisory Committee for guidance. Such determinations will be documented, communicated to stakeholders via e-mail and published on the Markit website www.markit.com/Product/Indices under the iTraxx News page. Where similar determinations are made, precedents set by previous decisions will be considered across all CDS indices.

In the unlikely instance an inaccuracy is not caught and resolved prior to the publication of the final list, or if input data used in the constituent selection process is revised retrospectively, Markit will review the impact on the affected indices. In order to determine whether to restate the final list or any index parameters, Markit will consult with the Index Advisory Committee to determine the impact of such action.

If it is decided to update the Final List or any related parameters, the reason for such revision together with revised material will be published. In addition, Markit will compile an incident report to summarize the incident, the root cause, and set forth remedial actions to avoid such an error in the future, where such remedial actions are applicable.

Publication of Annex

No later than three (3) Business Days prior to the Roll Date of a Markit iTraxx Japan Index, the Administrator will publish a draft of the annex for such Markit iTraxx Japan Index, along with the weighting and final reference obligations (if applicable) for each entity. The final annex for Markit iTraxx Japan Index will be published after 5:00 p.m. Tokyo Time on the Business Day immediately preceding the Roll Date of the Indices.

Changes to the Reference Obligations

In the event that the Administrator receives requests from three or more market participants that the reference obligation of an entity should be replaced, the Administrator will identify one new reference obligation for such entity, based on RED and on input from Markit iTraxx Japan Index market participants. A poll is then initiated by the Administrator. If a majority of the market participants participating in the poll agrees that such replacement

should be made, a new annex will be published by the Administrator, which will be identical to the previous annex, save for the fact that the reference obligation for such entity will be as agreed in the poll.

Changes to Entity Names

The treatment of all indices following corporate actions such as succession events is now governed by the amendment to the Small Bang protocol which was implemented by the ISDA Determinations Committee in December 2010. As per this amendment, as long as the effective date of the index is before the resolution date of an event by the relevant ISDA DC, it will be automatically taken into account without the need for reversioning the index or updating the index annex. The Administrator will not update the index annex for name changes and corporate actions in between roll dates.

Disclaimer

The Administrator does not undertake any duty of care and will not be liable to any party to a transaction referencing the Index for any form of damages, whether direct, indirect, special, consequential or otherwise, that might arise in connection with the Administrator's performance of its duties under the Rules, except in the case of the Administrator's gross negligence, fraud or wilful misconduct.

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